87-1392

No.

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE,

Appellant,

v.

DUDLEY TAYLOR, COMMISSIONER OF
REVENUE FOR THE STATE OF TENNESSEE,

Appellee.

On Appeal From The Supreme Court Of Tennessee

JURISDICTIONAL STATEMENT

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QUESTIONS PRESENTED

The State of Tennessee imposes an excise tax upon the net earnings of corporations doing business in Tennessee.Tenn. Code Ann. §§ 67-4-801 to 67-4-820. Prior to 1983, the State defined net earnings so as to include income earned on federal obligations and to exclude income earned on obligations of the State of Tennessee. In 1983, the excise tax statute was amended so that the definition of net earnings included income on both federal and Tennessee obligations.

The questions presented are:

I.

Whether the Tennessee Excise Tax Law is in violation of 31 U.S.C. § 3124 (which exempts from taxation by state or local authorities interest earned on obligations of the United States) when the 1983 amendment to the excise tax statute is invalid as an impairment of contract and violative of Article 1, Section 10, Clause 1 of the United States Constitution.

II.

Whether the Tennessee Excise Tax Law is in violation of 31 U.S.C. § 3124 when there exists a separate franchise tax imposed on all corporations, including banks, doing business in Tennessee, and therefore Tennessee imposes more than one tax on federal obligations.

III.

Whether the Tennessee Excise Tax Law is in violation of 31 U.S.C. § 3124 when it does not fit within the exceptions listed in Section 3124(a).

PARTIES TO THIS APPEAL

The Complaint as originally filed by First American National Bank of Knoxville contained allegations not only against the State of Tennessee Commissioner of Revenue, but also against county and city taxing authorities. The claims against the county and city taxing authorities were compromised and dismissed. The only parties before the Supreme Court of Tennessee were the appellant, First American National Bank, and the Commissioner of Revenue of the State of Tennessee. At the time of the proceedings in state court, the Commissioner of Revenue of the State of Tennessee was Martha B. Olsen. Since that time, the named appellee, Dudley Taylor, has succeeded Mrs. Olsen in that office; therefore, his name has been substituted as appellee in these proceedings.

The appellant First American National Bank of Knoxville has as its parent corporation First American Corporation of Nashville, Tennessee. Other wholly-owned subsidiaries of First American Corporation are as follows:

First American National Bank of Nashville

First Deaderick Corporation

FANB Corporation

Lee, Robinson, & Steine, Inc.

First American National Bank of Jackson

First American National Bank - Tri Cities

First American Bank of Memphis

(Formerly Midland Bank and Trust Company)

First Charlotte Corporation

First American Kentucky Bancorp, Inc.
First American Trust Company, N.A.
Ameristar Capital Markets, Inc.
First American Acquisition Corp. III
Guaranty Title Company
First American National Bank of Jefferson City
(Formerly First National Bank)
First American Bank - Greenback
First American Bank - McMinnville
First American Bank - Smyrna
First American Bank - Ashland
First and Peoples National Bank
First Amtenn Life Insurance Company
First and People's Trust Company

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE,

Appellant,

v.

DUDLEY TAYLOR, Commissioner Of
Revenue For The State Of Tennessee,

Appellee.

On Appeal From The Supreme Court Of Tennessee

JURISDICTIONAL STATEMENT

The appellant, First American National Bank of Knoxville ("First American"), appeals from a final judgment of the Supreme Court of Tennessee, entered November 23, 1987, upholding the validity of a Tennessee taxing statute, Tenn. Code Ann. §§ 67-4-801 to 67-4-820, which First American had challenged on the ground that as applied to it the statute violates the laws of the United States and is repugnant to the Constitution.

OPINIONS BELOW

The opinion of the Supreme Court of Tennessee, not yet reported, is reproduced in the Appendix hereto, pp. 1a-12a.

The Judgment of the Chancery Court of Knox County,Tennessee, entered on May 29, 1986, from which the appeal to the Supreme Court of Tennessee was taken, is not reported, but is reproduced in the Appendix, pp. 26a-28a. That Judgment incorporated by reference the main opinion of the court rendered on January 28, 1986, reproduced in the Appendix at pp. 13a-21a, and the court's opinion on post-trial motions rendered on May 8, 1986, reproduced in the Appendix at pp. 22a-25a.

JURISDICTION

The final judgment of the Supreme Court of Tennessee, Appendix, p. 29a, was entered November 23, 1987. That judgment upheld the validity of a Tennessee statute, Tenn. Code Ann. §67-4-806, challenged by First American as being in violation of the laws of the United States and repugnant to the Constitution. First American filed a Petition for Rehearing in the Supreme Court of Tennessee on December 3, 1987, which was withdrawn by agreement on December 29, 1987. The Notice of Appeal, Appendix, pp. 31a-32a, was filed in the Supreme Court of Tennessee on January 15, 1988. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(2).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

United States Constitution, Article, I, Section 10, Clause 1:

No state shall . . . pass any Law impairing the Obligation of Contracts . . . .

United States Constitution, Article VI, Clause 2:

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the *supreme Law of the Land*; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Tennessee Code Annotated § 67-4-806
Corporate Excise Tax

(a) All corporations, cooperatives, joint-stock associations, and business trusts, including regulated investment companies and real estate investment trusts, organized for profit under the laws of this state or any other state or country and doing business in Tennessee, including state chartered banks and national banks doing business in Tennessee shall, without exception other than as provided herein, pay to the commissioner of revenue, annually an excise tax, in addition to all other taxes, equal to six percent (6%) of the net earnings for the next preceding fiscal year for business done in this state.

(b) Every such taxable entity organized and existing under and by virtue of the laws of this or any other state, territory or country, or organized

and existing without any specific statutory authority, now or hereafter doing business within this state, without domesticating or qualifying to do business in this state, or while its charter is forfeited, revoked or suspended, shall as a recompense for the protection of its local activities and as compensation for the benefits it receives from doing business in Tennessee, pay the tax imposed by this part.

(c) The tax imposed by this part shall apply to corporations whose business is being conducted by a receivership or trusteeship appointed by any court of competent jurisdiction and shall continue to accrue until such time as the corporation has been actually and legally dissolved or withdrawn from this state.

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31 U.S.C. § 3124(a) Exemption from Taxation

(a) Stocks and obligations of the United States Government are exempt from taxation by a State or political subdivision of a State. The exemption applies to each form of taxation that would require the obligation, the interest on the obligation, or both, to ~~be~~ considered in computing a tax, except—

(1) a nondiscriminatory franchise tax or another nonproperty tax instead of a franchise tax, imposed on a corporation; and

(2) an estate or inheritance tax.

STATEMENT OF THE CASE

First American brought this action in the Chancery Court of Knox County, Tennessee, Part I, on March

11, 1983, to recover $135,000 in taxes paid under protest to Martha B. Olsen, Commissioner of Revenue of Tennessee.[1] The Complaint was subsequently supplemented so as to embrace further payments under protest. These taxes were assessed pursuant to the Tennessee Excise Tax Law, at Sections 67-4-801 to 67-4-820 (1983 Repl.) of the Tennessee Code Annotated. The specific section imposing the tax is Section 67-4-806, and is set out above at p. 3. The taxes sought to be recovered were for 1982 and 1983.

In 1982 and in years before that, the Tennessee corporate excise tax assessed a tax on the net earnings of all corporations doing business in Tennessee. The term "net earnings" was, at that time, so defined as to exclude income earned from obligations of the State of Tennessee and to include income earned from obligations of the federal government. In 1983, the excise tax was amended by the Tennessee legislature in an attempt to conform to the ruling of this Court in *Memphis Bank & Trust Co. v. Garner*, 459 U.S. 392 (1983), which held that the Tennessee Bank Tax, which similarly defined net earnings, impermissibly discriminated against the federal government in violation of 31 U.S.C. § 742 [now 31 U.S.C. § 3124], by excluding income from Tennessee obligations in the bank tax base while including income from federal obligations in that tax base.

In its Complaint, as supplemented, First American alleged that the excise tax, as applied to it, was in violation of 31 U.S.C. § 3124 both before and after

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[1] The original Complaint contained another count regarding the Tennessee Bank Excise Tax. Tenn. Code Ann. §§ 67-751 to 67-763. This issue was not part of the appeal to the Supreme Court of Tennessee, and is not before this Court.

the tax was amended (Amended Complaint for the Recovery of Taxes Paid Under Protest, paragraphs 13 and 15), and was thus unconstitutional under the Supremacy Clause of the United States Constitution.

The case was tried on September 30 and October 1, 1985. The trial court agreed with First American that before amendment the excise tax suffered from the same infirmity as did the bank tax at issue in *Memphis Bank & Trust*. With regard to the excise tax as amended in 1983, however, the trial court found that the amendment removed the discriminatory treatment of federal obligations and did not impair the obligation of contracts and ruled against First American on that issue. Appendix, pp. 20a-21a.

First American appealed to the Supreme Court of Tennessee, arguing that the excise tax, even as amended, remained discriminatory, because the Tennessee legislature's amendment attempted to tax for the first time Tennessee obligations issued before 1983. First American argued this would be an impairment of contract and invoked both the United States and Tennessee Constitutions. Further, First American argued that the excise tax was in violation of 31 U.S.C. § 3124 because Tennessee imposed an additional tax on federal obligations under its franchise tax, which was not challenged. Additionally, it was argued that the Tennessee excise tax violated 31 U.S.C. § 3124 because it did not fit any of the exceptions listed by that statute. The Tennessee Supreme Court affirmed, holding that the amended excise tax did not violate 31 U.S.C. § 3124, or the United States Constitution. Appendix, pp. 11a-12a. The Court reasoned that the attempt by the Tennessee legislature to tax Tennessee obligations issued

prior to 1983, which were not taxable when issued, was not an impairment of contract. Appendix, pp. 6a-7a. The Court went on to hold that a state was not limited by 31 U.S.C. § 3124(a) to a single tax affecting federal obligations. Appendix, pp. 8a-11a. The Tennessee Supreme Court also held that the corporate excise tax did not violate 31 U.S.C. § 3124(a) because it fit one of the taxation exemptions permitted by that statute. Appendix, pp. 10a-11a. In sum, the Supreme Court of Tennessee "found no Constitutional barrier to the 1983 amendment . . . ." Appendix, p. 11a.

THE QUESTION IS SUBSTANTIAL

It was in the early days of the Republic that this Court decided that states could not tax obligations of the federal government. *Weston v. City Council of Charleston*, 2 Pet. (27 U.S.) 449 (1829). This rule was, and is, essential to the protection of the borrowing power of the United States. *See Society for Savings in the City of Cleveland v. Bowers*, 349 U.S. 143, 144 (1955). Congress enacted this rule in 1862, 12 Stat. 346, and it remained substantially unchanged until 1959, when Congress reacted to attempts by the states to circumvent the rule by taxing indirectly federal obligations by amending the statute expressly to state that:

> This exemption extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other non-property taxes in lieu thereof imposed on cor-

> porations and except estate taxes or inheritance taxes.

31 U.S.C. § 742; *see* S. Rep. No. 909, 86th Cong., 1st Sess. ___, *reprinted in* 1959 U.S. Code Cong. & Ad. News 2769, 2773-74.

Congress dealt with an attempt by several states to tax federal obligations not by taxing the obligation itself, but by "measuring" the tax by the value of the obligation and income derived from them. *Public Debt Ceiling and Interest Rate Ceiling on Bonds: Hearings Before the House Committee on Ways and Means*, 86th Cong., 1st Sess., (1959) (Statement of Hon. Robert B. Anderson, Secretary of the Treasury). This attempt was, of course, recognized as a red herring by Congress, and eventually, by this Court. *See First National Bank of Atlanta v. Bartow County*, 470 U.S. 583 (1985).

The rule of non-taxability of federal obligations was confirmed by this Court's decision in *Memphis Bank & Trust Co. v. Garner*, 459 U.S. 392 (1983). In that case, this Court held that the Tennessee Bank Excise Tax "impermissibly discriminate[d] against the Federal Government and those with whom it deals." *Id.* at 399. Recognizing that the Tennessee Excise Tax Law defined "net earnings" in the same way as did the Bank Tax, and therefore was subject to challenge under *Memphis Bank & Trust*, the Tennessee Supreme Court held the excise tax law invalid in *Midland Bank & Trust v. Olsen*, 717 S.W.2d 580 (Tenn. 1986), *cert. denied*, 107 S.Ct. 1336 (1987). Anticipating this, the Tennessee legislature amended the excise tax so as to attempt to tax obligations of the State of Tennessee. First American contended below, and would assert to this Court, that this attempt was

ineffective, and therefore the statute continues to discriminate against federal obligations and is invalid.

The attempt by the Tennessee legislature to tax Tennessee obligations is invalid because to do so would result in an unconstitutional impairment of contract. The Tennessee obligations were issued in 1982 and years prior. First American, along with many others, bought these bonds with the understanding that they would produce tax exempt income. This was undisputed by the State of Tennessee at trial. To attempt to tax the income from these obligations after having sold them by the inducement that they would not be subject to tax clearly constitutes an impairment of contract in violation of Article I, Section 10, Clause 1 of the United States Constitution. The Tennessee Supreme Court decided that this did not constitute an impairment of contract. Appendix, pp. 6a-7a. In so holding, the court reasoned that the excise tax was a tax on the privilege of doing business in the corporate form, and not a tax directly or indirectly on the obligations themselves. The tax, so the rationale goes, is thus merely *measured by* state obligations (and, of course, federal obligations) and not a tax *on* state obligations; therefore, there is no impairment of contract. Appendix, pp. 6a-7a.

Respectfully, the Tennessee Supreme Court relied upon the anachronistic formalistic distinction thought to be laid to rest in *First National Bank of Atlanta v. Bartow County*, 470 U.S. 583 (1985). In that case, this Court, in reviewing the legislative history of 31 U.S.C. 742 (now 31 U.S.C. § 3124(a)) thought it clear "that Congress intended to abolish the formalistic distinction between taxes *on* income and taxes *measured by* income . . . ." 470 U.S. at 594. In spite of this,

the Tennessee court used this outdated bit of semantic misdirection in an attempt to salvage the excise tax. The fact is, however, that before 1983, there was no excise tax imposed by Tennessee either *on* Tennessee obligations or *measured by* Tennessee obligations. The contract that existed at the time the Tennessee obligations were purchased by First American was that the Tennessee obligations would not be included in the corporate excise tax base—they would neither be taxed nor used to measure the tax. After the 1983 amendment, the Tennessee obligations were included in the tax base and so there was a tax *on* or *measured by* Tennessee obligations. This is an impairment of contract. As set out in *Lake County v. Morris*, 160 Tenn. 619, 28 S.W.2d 351 (1930), the test of impairment of a state obligation is whether the value of the contract or security has been lessened. It is beyond dispute that making taxable a previously nontaxable asset reduces the market value of that asset; therefore, the contract of purchase has been impaired. *See, e.g., Moore v. Otis*, 275 F. 747 (8th Cir. 1921).

Since First American's contract with the State of Tennessee has been impaired by the 1983 amendment to the excise tax law, that amendment is invalid under Article I, § 10, Clause 1 of the United States Constitution, and cannot be given effect. This being so, the result is that Tennessee obligations purchased prior to the 1983 amendment are not included in net earnings for purpose of the excise tax, and federal obligations are included; therefore, the tax is not nondiscriminatory as required by 31 U.S.C. § 3124(a) and cannot stand.

The Tennessee Excise Tax Law is invalid for other reasons as well. First, section 3124(a) says that fed-

eral obligations are not taxable except for "*a* nondiscriminatory franchise tax or another nonproperty tax *instead of a* franchise tax . . . ." [Emphasis added.] The appellant contends that this means one tax and one tax bite on federal obligations is all Tennessee is allowed. The Tennessee Supreme Court held to the contrary:

> As far as we have been able to discover, this language has never been so construed to limit the States' taxing authority; moreover, we think that the usage of the indefinite article ("a" or "an") does not carry the connotation proposed by Plaintiff and means only "any" tax within the statutory exception.

___ S.W.2d ___ (Appendix, p. 9a) (footnote omitted). First American respectfully disagrees. Up until 1959, the statute, then 31 U.S.C. § 742, made federal obligations absolutely exempt from state taxation. Act of February 25, 1862, ch. 33, § 2, 12 Stat. 346. The 1959 amendment, Pub. L. 86-346, 73 Stat. 622, provided an exception for "nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations . . . ." *Id.*, (codified as 31 U.S.C. § 742). In 1982, the language of the statute was again amended to substitute "instead" for "in lieu" for clarity. *See* Explanatory Note to 31 U.S.C. § 3124.[2] The 1959 amendment had as one of its purposes to give the states more leeway in producing revenue. Congress cannot have intended, however, for the states to be allowed taxes without number, even assuming that the taxing statutes would otherwise satisfy sec-

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[2] Title 31 has now been enacted into positive law. Pub. L. 97-258, 96 Stat. 877.

tion 3124(a). Such a result would reduce to nothing the value of federal obligations, thereby destroying the power of the federal government to raise revenue by borrowing money. The credit of the government of the United States would be worthless. As this Court stated many years ago, "[T]he power to tax involves the power to destroy . . . ." *M'Culloch v. Maryland*, 4 Wheat. (U.S.) 316 (1819).

" 'Absent a clearly expressed legislative intention to the contrary, [the statutory] language must ordinarily be regarded as conclusive.' " *American Bank & Trust Company v. Dallas County*, 463 U.S. 855, 862 (1983). The language of § 3124(a) is clear and unambiguous and prohibits all taxation except "a nondiscriminatory franchise tax or another nonproperty tax instead of a franchise tax, imposed on a corporation . . . ." The Tennessee Supreme Court sanctioned this approach, to have a corporate excise tax in *addition* to its separate franchise tax as codified at Tenn. Code Ann. §67-4-901 to 67-4-918. Appendix, pp. 9a-10a. The Tennessee Supreme Court voided the statutory restriction of 31 U.S.C. § 3124(a) by lumping the excise and franchise taxes together as one "scheme of taxation." Appendix, p. 9a. This interpretation by the Tennessee Supreme Court to uphold the validity of the corporate excise tax as amended is contrary to the language of 31 U.S.C.§ 3124(a) and is beyond the exception provided for by §3124(a).

Whether the excise tax in question is a "franchise" tax under section 3124(a) has not been decided by this Court. First American submits that this is a question to be governed by federal, not Tennessee, law—*see Society for Savings v. Bowers*, 349 U.S. 143, 151 (1955)—and under federal law the Tennessee Excise

Tax is not a franchise tax. Even though it may not have been so earlier, by 1959 when Congress amended section 742 (now § 3124(a)), the terms "franchise" and "excise" had acquired discrete meanings. A franchise tax was a tax on net worth; an excise tax was a tax on net earnings. *See Werner Machine Co. v. Director of Taxation*, 350 U.S. 492, 493-94 (1956). Congress must be presumed to have known what it was doing, then, when it excepted only franchise, estate, and inheritance taxes from the general prohibition of section 742. Congress must be understood to have provided exceptions for state taxes based on net worth or value of federal obligations. A tax on net earnings, or on income, is prohibited. The Tennessee excise tax is a corporate income tax, the Tennessee Supreme Court's holding to the contrary notwithstanding. Tennessee already has a "franchise" tax, which it describes as a tax on the privilege of doing business in the corporate form in Tennessee. To say that the excise tax is really just another franchise tax is unreasonable.

Neither is the excise tax a nonproperty tax instead of a franchise tax. As seen above, Tennessee already has a franchise tax; therefore, even if the excise tax could be classified as a nonproperty tax, it would be in addition to, rather than instead of the franchise tax.

The foregoing description of the issues involved in this appeal understates their importance. If the Tennessee Supreme Court's interpretation of federal constitutional and statutory law involved is allowed to stand, it can reasonably be expected that other states will impose both retroactive and prospective addi-

tional taxes on federal obligations.[3] Because many, if not all, states are financially strapped, it is not far-fetched to anticipate that the number of new taxes enacted will substantially impair the ability of the federal government to borrow money. This unwarranted interference with the fiscal health of the federal government cannot be allowed. To allow the holding of the Tennessee Supreme Court to stand so as to circumvent both the United States Constitution and section 3124(a) would encourage states in times of financial difficulty to ignore the Constitution and United States statutes and to enact additional prohibited taxes. The importance of these issues warrant plenary consideration by this Court, with briefs on the merits and oral argument.

CONCLUSION

For these reasons, this Court should note probable jurisdiction of this appeal.

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[3] For example, in the last four months, two state supreme courts have upheld state taxes on federal obligations. *Centerre Bank of Crane v. Director of Revenue*, No. 69047 (Mo. Jan. 20, 1988); *Department of Revenue v. First Union National Bank*, 513 So.2d 114 (Fla. 1987), *appeal docketed*, No. 87-1074 (U.S. Dec. 23, 1987).

Respectfully submitted,

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APPENDIX

IN THE SUPREME COURT OF TENNESSEE

AT KNOXVILLE

FIRST AMERICAN NATIONAL BANK OF KNOXVILLE (PARK NATIONAL BANK),

Plaintiff-Appellant,

v.

MARTHA B. OLSEN, COMMISSIONER OF REVENUE FOR THE STATE OF TENNESSEE,

Defendant-Appellee.

FOR PUBLICATION

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Knox Equity

S/C No. 270

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OPINION

AFFIRMED.
DROWOTA, J.

In this tax refund suit, involving two consolidated cases,[1] Plaintiff seeks a refund of corporate excise taxes paid under protest for the tax year 1983. Plaintiff contends that the amended excise tax, T.C.A. §§67-4-801, *et seq.*, violates 31 U.S.C. §3124(a) and impairs the obligation of a contract. Further, Plaintiff alleges that the trial court erred in disallowing the calculation of its 1982 net operating loss to be carried over into the 1983 tax year.

The genesis of this lawsuit is found in this Court's decision in *Memphis Bank & Trust Co. v. Garner*, 624 S.W.2d 551 (Tenn. 1981) (*Garner I*), *reversed and remanded* 459 U.S. 392, 103 S.Ct. 692 (1983). In *Memphis Bank & Trust Co. v. Garner*, 459 U.S. 392, 103 S.Ct. 692 (1983) (*Garner II*), the United States Supreme Court held that the Ten-

[1] Initially, three cases were consolidated but one was settled. The two remaining cases involve Park National Bank and First American National Bank of Knox County, which merged in November, 1983. They are referred to as Plaintiff. First American National Bank was the surviving corporation in the merger.

nessee local bank excise tax, T.C.A. §§67-751, *et seq.* (now repealed),[2] unconstitutionally discriminated against Federal obligations because the interest from such obligations was included in the tax base while the interest on the obligations of the State of Tennessee was not included, thereby violating 31 U.S.C. §742 (now codified as 31 U.S.C. §3124). Upon remand, this Court issued an unpublished opinion, *Memphis Bank & Trust Co. v. Garner* (filed February 27, 1984; *per curiam*) (*Garner III*), which conformed to the holding of the United States Supreme Court. Subsequent to the opinion in *Garner II*, the Tennessee Legislature amended the Tennessee Corporate Excise Tax, T.C.A. §§67-4-801, *et. seq.*, to cure the same discriminatory treatment of Federal obligations found in the local bank tax act, which the Legislature repealed, by including Tennessee obligations in the excise tax base under T.C.A. §67-4-805 (Supp. 1987) and thus treating Federal and State obligations in a nondiscriminatory fashion. *See Midland Bank & Trust Co. v. Olsen*, 717 S.W.2d 580, 582 (Tenn. 1986), *cert. denied*, _____U.S. _____, 107 S.Ct. 1336 (1987).

Plaintiff's predecessor, Park National Bank, and First American National Bank paid their 1983 corporate excise taxes under protest and on March 11, 1983, filed a Complaint in the Chancery Court for Knox County, seeking a refund of 1983 excise taxes.[3] A number of amendments to the Complaint followed to include subsequent payments of taxes under protest and on September 30 and October 1, 1985, the trial of this action was held. On January 28, 1986, Chancellor Frederick McDonald filed his Memorandum Opinion in which he determined that the corporate excise tax was properly imposed in 1983. Finding that the Legislature's inclusion of the interest on Tennessee obligations in Plaintiff's net earnings did not impair the ob-

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[2] Chapter 227, §1, 1983 Public Acts.

[3] A refund of certain 1982 taxes was also sought and recovered; this is not an issue in this case.

ligation of a contract because the tax was not imposed on these obligations but was merely measured by the income of the corporation, which income included interest earned on government obligations, the Chancellor ruled that no refund of 1983 taxes was due. Following a Motion for Further Findings of Fact and Conclusions of Law, the trial court again issued a Memorandum Opinion on May 8, 1986, which did not substantially alter the January 28, 1986, rulings, and Judgment was entered on May 25, 1986. Notice of Appeal was duly filed. We now affirm.

The issues on appeal are: (1) Whether the Tennessee Corporate Excise Tax, as amended in 1983, violates 31 U.S.C. §3124(a) because the amendment was ineffective to cure discrimination against Federal obligations; (2) Whether the corporate excise tax is a franchise or nonproperty tax within the meaning of 31 U.S.C. §3124(a)(1); and (3) Whether the Plaintiff is required to include interest on government obligations in computing its 1982 net operating loss carryover for the purpose of its 1983 excise taxes. These issues are purely legal and no factual dispute exists in this case.

Plaintiff argues that the 1983 amendment to T.C.A. §67-4-805 is ineffective because it conflicts with T.C.A. §9-9-112, which exempts State obligations from taxation (with certain exceptions inapplicable in this case), and other similar provisions. The tax exemption provided by these sections, being specific, controls the general excise tax statutes and thus revives the discriminatory treatment of Federal obligations held unconstitutional in *Garner II* and *Garner III*. Moreover, Plaintiff also contends that the 1983 amendment to the Tennessee Corporate Excise Tax breaches and impairs the obligation of its contracts with the State, formed when it purchased these tax exempt obligations prior to the amendment, and imposes the excise tax retroactively upon State obligations, violating the Constitutions of the State of Tennessee and of The United States.

Although Plaintiff and Amici make a sophisticated argument in support of their contentions on this issue, we are not persuaded that the 1983 amendment to the excise tax either violates 31 U.S.C. §3124(a) or impairs the obligation of a contract. The discriminatory treatment condemned in *Garner II* is not revived by any perceived conflict among T.C.A. §67-4-805, as amended, and such statutes as T.C.A. §9-9-112. As this Court concluded in a similar case, construing a forerunner to this present code section, T.C.A. §9-9-112 "does not exempt appellant corporation from the payment of the privilege tax enacted by the State for the privilege of doing business in Tennessee. . . ." *National Life & Accident Ins. Co. v. Dempster,* 168 Tenn. 446, 457-458, 79 S.W.2d 564, 568 (1934). The excise tax is not aimed at or based solely on earnings from tax exempt obligations of the State or its political subdivisions. *Id.,* 168 Tenn. at 456, 79 S.W.2d at 567. Because no inconsistency exists among the amended excise tax and the statutes providing a tax exemption for State obligations, application of the rules of statutory construction regarding conflicting statutory enactments is inappropriate and unnecessary; the statutes may be enforced together as they stand. The tax exemption for such obligations is not affected now anymore than when *Dempster* was decided: "By the act in question [the State] has adopted a form of privilege tax on corporations measured by their net income, without any form of discrimination as to the sources of the income included in the measure. . . ." *Id.,* 168 Tenn. at 455, 79 S.W.2d at 567. Since no conflict among the statutes at issue revives a tax exemption for the State, no discriminatory treatment is recreated contrary to the requirements of *Garner II* and 31 U.S.C. §3124(a).

> "Having guaranteed to the purchasers of these bonds immunity from taxation of the principal and interest, the State of Tennessee is without power subsequently to destroy the immunity and

> to tax the bonds or interest directly or indirectly. The act here in question, however, does not tax either the principal or interest of any bonds of the State of Tennessee, or of any political subdivision thereof, or of the United States."

Dempster, supra, 168 Tenn. at 456, 79 S.W.2d at 568. The 1983 amendment was explicitly enacted to include Tennessee obligations in the measure of the excise tax and this legislative intent must be upheld absent a constitutional barrier. "The power of determining the measure of the tax is a legislative function." *Bank of Commerce & Trust Co. v. Senter,* 149 Tenn. 569, 592, 260 S.W. 144, 150 (1923).

For similar reasons, the amended excise tax, which requires the taxpayer to include the earnings from tax exempt obligations of the State, of its political subdivisions, and of the United States, in the calculation of net income, does not impair the obligation of the contracts formed when State obligations were purchased. The Tennessee Constitution, Art. I, §20, and the Constitution of the United States, Art. I, §10, cl. 1, both prohibit laws that impair the obligation of a contract; however, the contracts between the State and Plaintiff are not impaired by inclusion of income from such obligations in the tax base on which the excise tax is imposed because "[t]he owner may enjoy his exempt property free of tax, but if he asks and receives from the State the benefit of a taxable privilege as the implement of that enjoyment, he must bear the burden of the tax which the State exacts as its price." *Pacific Co., Ltd. v. Johnson,* 285 U.S. 480, 490, 52 S.Ct. 424, 426 (1932). The excise tax is not imposed directly or indirectly on the obligations themselves or on the income earned from them but rather on the privilege of utilizing the corporate form in Tennessee, regardless of whether a corporation uses that privilege to acquire tax exempt obligations, *id.,* 285 U.S. at 490, 52 S.Ct. at 426; it does not revoke the tax immunity provided by such statutes as

T.C.A. §9-9-112. Thus, the obligation of the contracts formed with Plaintiff at the time of their purchase is not impaired. "[T]he principle on which the doctrine of non-impairment of contracts stands is, that the law for its enforcement and execution existing at the time makes a part of the contract, so enters into it as to become a part of it, and therefore stands protected by the constitutional inhibition." *Corporation of Knoxville v. Bird,* 80 Tenn. 121, 124 (1883). The *Dempster* case previously established as a part of the applicable law that a tax on the privilege of doing business as a corporation does not conflict with the tax exemption provided for Tennessee obligations. The Legislature could not retroactively revoke the tax exemption for such obligations or otherwise impose a tax upon such obligations or the income earned on them, but that is not what the amended excise tax does. *See, e.g., Dempster, supra,* 168 Tenn. at 456, 79 S.W.2d at 568. The tax is imposed on the privilege of incorporation and is measured by the corporation's net income, as defined and calculated in the excise tax statutes and regulations.

The next issue concerns the nature of the excise tax and whether it is within the taxation exceptions permitted by 31 U.S.C. §3124(a), which provides:

> "Stocks and obligations of the United States Government are exempt from taxation by a State or political subdivision of a State. The exemption applies to each form of taxation that would require the obligation, the interest on the obligation, or both, to be considered in computing a tax, except —
>
> (1) a nondiscriminatory franchise tax or another nonproperty tax instead of a franchise tax, imposed on a corporation; and
>
> (2) an estate or inheritance tax."

Plaintiff asserts that since Tennessee already has a franchise tax, T.C.A. §§67-4-901, *et seq.,* which Plaintiff has

paid, the excise tax cannot be imposed as well if income from United States obligations is included in the tax base because 31 U.S.C. §3124(a) permits only one State tax on such obligations; regardless, Plaintiff insists that the excise tax nevertheless constitutes an income tax and thus is not within the taxation exceptions allowed by the Federal statute.

Unlike any of the *Garner* cases, the issue presented here is not whether the tax is discriminatory but rather whether the excise tax can be imposed in addition to a franchise tax and whether the excise tax constitutes an income tax for the purposes of 31 U.S.C. §3124(a). The Tennessee Corporate Excise Tax has long been held to be a privilege tax. *See, e.g., Broadmoor-Kingsport Apartments, Inc. v. State,* 686 S.W.2d 70, 72 (Tenn. 1985); *Roane Hosiery, Inc. v. King,* 214 Tenn. 441, 445-446, 381 S.W.2d 265, 267 (1964); *Bank of Commerce & Trust Co. v. Senter, supra,* 149 Tenn. at 582-583, 260 S.W. at 146-147. Moreover, the excise and franchise taxes have also been consistently construed together as one coordinate scheme of taxation. *See, e.g., American Bemberg Corp. v. Carson,* 188 Tenn. 263, 272, 219 S.W.2d 169, 173 (1949). In *Garner I,* this Court expressly rejected "the taxpayer's argument that the term 'franchise' tax used in the federal statute excludes a general corporate 'excise' tax." 624 S.W.2d at 554. *Garner II* did not address this issue, which was expressly noted by this Court in *Garner III;* rather, in *Midland Bank & Trust Co. v. Olsen, supra,* we concluded that the United States Supreme Court impliedly characterized the local bank excise tax as a nonproperty tax for the purposes of 31 U.S.C. §3124(a). 717 S.W.2d at 583, n. 3. Accordingly, we continue to hold that the corporate excise tax is also a nonproperty tax for the purposes of this Federal statute; it is imposed not on the income itself but, as noted previously, on the privilege of doing business in Tennessee in the corporate form. The Legislature has also explicitly stated that this is the policy of the excise tax in T.C.A.

§67-4-806(b). The United States Supreme Court itself has recently recognized that 31 U.S.C. §3124(a) "did not prohibit nondiscriminatory taxes imposed on discrete property interests such as corporate shares or business franchises, even though the value of that discrete interest was measured by the underlying assets, including United States obligations." *American Bank & Trust Co. v. Dallas County*, 463 U.S. 855, 858, 103 S.Ct. 3369, 3372 (1983) (citations omitted). The Tennessee Franchise Tax, T.C.A. §§67-4-901, *et seq.*, is imposed on a different tax base than the Corporate Excise Tax, T.C.A. §§67-4-801, *et seq.*, but both expressly provide that the taxes are to be paid "in addition to all other taxes." T.C.A. §§67-4-806 (Supp. 1987); 67-4-903. The Legislature clearly intends that these taxes be taken in tandem and construed together as one scheme of taxation.

Plaintiff relies on the Federal statutory language, emphasizing that "[t]he exemption applies to each form of taxation that would require the obligation, the interest on the obligation, or both, to be considered in computing *a* tax, except - (1) *a* nondiscriminatory franchise tax or another nonproperty tax *instead* of *a* franchise tax, imposed on a corporation" (emphasis added), and argues that this language permits the State to impose only one such tax. As far as we have been able to discover, this language has never been so construed to limit the States' taxing authority; moreover, we think that the usage of the indefinite article ("a" or "an") does not carry the connotation proposed by Plaintiff and means only "any" tax within the statutory exception.[4] Consequently, a number of acceptable forms of taxation can be imposed within this exception and we do not think that such a significant

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[4] *Webster's Third New International Dictionary (Unabridged)* includes in the uses of the indefinite article, "a", the connotations "any" or "each", which usages are directly contrary to the construction of the Federal statute for which Plaintiff here contends.

limitation on the taxing authority of the States should be readily inferred from this statutory language without a more definite expression of Congressional intent. Otherwise, as the United States Supreme Court has observed in a somewhat different context:

> "Were federal obligations permitted to shelter taxable assets, the States likely would be unable to raise worthwhile revenues through bank share taxes. In that event, one would expect that the States would move to tax banks through franchise or other nonproperty taxes specifically excepted from the proscriptions of [31 U.S.C. §3124]."

First National Bank of Atlanta v. Bartow County Board of Tax Assessors, _____U.S. _____, _____, 105 S. Ct. 1516, 1524 (1985).

We think that Congress simply intended that Federal obligations and the interest thereon cannot "be considered in computing" any tax *except* (as relevant here) nondiscriminatory franchise or other nonproperty taxes such as an excise tax; these obligations thus can be considered in computing nondiscriminatory taxes that fall within the exceptions provided by 31 U.S.C. §3124(a). "Congress must have believed that franchise . . . taxes required federal obligations to 'be considered, directly or indirectly, in the computation of the tax'; otherwise, the specific exemption for these taxes would have been superfluous." *American Bank & Trust Co. v. Dallas County, supra*, 463 U.S. at 864, 103 S. Ct. at 3375. In a related fashion, Plaintiff has argued that the distinction between a tax *on income* and a tax *measured by income* has been abolished by 31 U.S.C. §3124, citing *First National Bank of Atlanta v. Bartow County, supra*, 105 S. Ct. at 1523, but we must conclude from the foregoing discussion that this distinction survives for any State taxes within the Federal statutory exceptions. *See American Bank & Trust Co. v. Dallas County,*

supra, 463 U.S. at 858 and 867, 103 S. Ct. at 3372 and 3377. As this Court observed in *Bank of Commerce & Trust Co. v. Senter, supra*, "a tax must be measured by some standard, and the right to select the measure devolved upon the legislative department, and . . . their selections [are] valid unless constitutional limitations [are] overstepped." 149 Tenn. at 584, 260 S.W. at 148. Thus, we also reject Plaintiff's contention that the excise tax is an income tax for the purposes of 31 U.S.C. §3124(a).

The Plaintiff's final issue concerns the disallowance of its calculation of the carryover of its 1982 net operating loss to the 1983 tax year. Fundamentally, Plaintiff argues that it is not required to include its 1982 income from Tennessee and Federal obligations in calculating its net operating loss carryover, resulting in a loss, and to require inclusion constitutes taxation of 1982 income from such obligations in 1983 in violation of 31 U.S.C. §3124(a).

The answer to this contention is relatively simple. T.C.A. §67-4-805(2)(c) is intended to permit the carryover of actual economic losses and thus all taxable income is included in determining whether such an actual loss exists for excise tax purposes. In *Union Planters National Bank v. Woods*, 590 S.W.2d 455 (Tenn. 1979), this Court invalidated a pre-1976 regulation promulgated by the Commissioner of Revenue that required inclusion of total income (including earnings from State and Federal obligations) in the calculation of net operating loss, but in 1976 the Legislature essentially adopted the Commissioner's pre-1976 regulation in an amendment to the excise tax statute. This nondiscriminatory treatment of State and Federal obligations is consistent with the requirements of 31 U.S.C. §3124(a). We think it evident that the Legislature intended net operating losses for the purpose of the carryover provision to reflect actual economic losses.

Accordingly, having found no Constitutional barrier to the 1983 amendment, we affirm the judgment of the Chan-

cery Court of Knox County. As the Supreme Court of the United States noted in *Bartow County, supra*, "[t]he tax exemption required by the Constitution and [31 U.S.C. §3124(a)] is not a tax shelter." 105 S. Ct. at 1524. The costs are taxed to the Plaintiff.

/s/Frank F. Drowota, III
FRANK F. DROWOTA, III, Justice

Concur:

Harbison, C.J.
Cooper and O'Brien, JJ
Cantrell, Sp. J.

IN THE CHANCERY COURT
FOR KNOX COUNTY TENNESSEE

PART I

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE (PARK NATIONAL BANK),
Plaintiff

vs. No: 78471

MARTHA B. OLSEN, Commissioner
of Revenue for the State of
Tennessee, et al

Defendants,

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE (FIRST AMERICAN
BANK OF KNOX COUNTY),

Plaintiff

vs. No: 79581

ROBERT BROOME, Knox County
Trustee, et al

Defendants

MEMORANDUM OPINION

The above two cases for recovery of taxes have been consolidated for trial. In case number 78471 First American National Bank of Knoxville brings suit to recover taxes paid by the Park National Bank, which is now merged into Plaintiff. In that case recovery of the following taxes is sought:

(a) 1982 bank excise taxes paid pursuant to T.C.A. 67-751 et seq., the bank having paid under the minimum payment provision of T.C.A. 67-752, and

(b) 1982 and 1983 corporate excise taxes, paid under T.C.A. 67-2701 et seq. (now T.C.A. 67-4-801 et seq.) By stipulation of the parties taxes paid after 1983 taxes are no longer to be considered in this suit.

In case number 79581 the First American National Bank, in a claim unrelated to the old Park National Bank, seeks recovery of 1982 bank excise taxes paid by the former First American Bank of Knox County, which is also now merged into Plaintiff.

Another case, number 79879, brought by the Third National Bank, had been consolidated for trial with these cases, but that case has been settled, and no longer is before the Court for decision.

The first question to be addressed is the defense contention that the taxes were voluntarily paid, and therefore not recoverable. The involved taxes were paid under protest; however, prior to having become delinquent administrative steps were taken to collect the taxes: the assets, liabilities and earnings of the banks were reviewed by the taxing authorities, who then determined the amount of taxes claimed due. In particular, a certification of the bank excise taxes claimed due was prepared by the Tennessee Comptroller of the Treasury, Division of Property Assessment certifying the 1982 taxes due pursuant to T.C.A. 67-751 eq [sic] seq.; it was forwarded to the local authorities, and in accord therewith the city and county sent statements for the claimed taxes to the banks, who paid the taxes [sic] liability asserted under protest.

T.C.A. 67-1-901, which provides for payment under protest, conditions such payment upon circumstances where any proceeding is instituted, or steps are taken for collection of the sum claimed due. Here, administrative steps were taken to collect the taxes as already noted.

More recent Tennessee cases considering the question of voluntariness of tax payments have recognized the im-

plied duress under which the payment of a tax is almost always made. *Sky Transpo, Inc.* vs. *City of Knoxville* (Tenn S. Ct., Dec. 30, 1985), and cases cited therein. In *Bell* vs. *Clay County,* 168 Tenn 6, 73 SW2d 685 (1934), the Court spoke of duress as that which is sufficient to create an urgent and immediate necessity to pay. For a bank, indeed, for any taxpayer, the need to avoid becoming delinquent generally will create such urgent and immediate necessity. If the Tennessee tax statute were to be applied as the defense requests, it might be deemed to provide an inadequate remedy, permitting relief in federal court. *Matthews* vs. *Rodgers* 284 US 521 (1931); *Aluminum Co. of Am.* vs. *Dept. of Trea.* 522 F2d 1120 (6th Cir 1975). It is concluded that with one exception, the taxes here were paid involuntary and under protest, so that Plaintiff may contest their validity. The mentioned exception is the corporate excise tax paid July 14, 1983 in the amount of $42,000.00, which was not paid under protest, and therefore is not recoverable; as will be seen, however, this conclusion makes no difference to the final outcome of the case.

To facilitate a better understanding of this litigation the distinction between the Tennessee corporate excise tax, and the Tennessee bank excise tax should be explained. The corporate excise tax imposed under T.C.A. 67-2701 et seq. (now 67-4-801 et seq.) generally applies to all corporations, and until 1983, when it was amended to respond to rulings of the Supreme Courts of the United States and Tennessee, all of the revenue it produced went to the State. The bank excise tax imposed under T.C.A. 67-751 et seq. applied to banks only; the revenue from it went to local governments, and it was repealed in 1982. The Supreme Court observed in *Commerce Union Bank* vs. *State Bd. of Equalization,* 615 SW2d 151 (Tenn 1981):

> "... the bank excise tax is to be calculated in the same manner as the general corporate excise

> tax and is really nothing more than an additional excise tax payable to local governments."

First, the right of plaintiff bank to recover the involved 1982 bank excise taxes will be considered. Plaintiff primarily relies upon *Memphis Bank and Trust Co.* vs. *Garner,* 459 US 392, 74 LED 2d 562, 193 S Ct 692 (1983). In that case the United States Supreme Court held the Tennessee bank excise tax violated 31 USC Section 742. That federal statute permits very limited, nondiscriminatory, franchise and other nonproperty state taxes on corporations with respect to federal securities, and excludes all other direct or indirect state and local taxation of federal securities. Section 742 of the federal act provides:

> "Except as otherwise provided by law, all stocks, bonds, Treasury notes, and other obligations of the United States, shall be exempt from taxation by or under State or municipal or local authority. This exemption extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations and except estate taxes or inheritance taxes."

In the *Garner* case the United States Supreme Court concluded that the Tennessee bank excise tax discriminated in favor of Tennessee securities, and against federal securities. This was because income from federal obligations was considered in computing the tax, but income from Tennessee bond and other state obligations was not. This occurred because the bank excise tax was computed in the same manner as the Tennessee corporate excise tax, which was and still is computed on net corporate earnings, which are basically defined as "federal taxable income" which includes income from federal obligations. However, it does

not include income from state obligations. 26 USC, Section 103 (a)(1). Thus federal security income, being considered in computing the tax, the exclusion of state security income therefrom constituted discrimination against federal securities under 31 USC, Section 742, and rendered the tax invalid.

The bank excise taxes sought to be imposed in this case are discriminatory against federal securities as was the case in *Garner*, and for the same reasons. The computation of the tax requires consideration of federal security income, but not state income. This is impermissible discrimination under 31 USC, Section 742, and renders the taxes sought to be imposed in this case invalid.

The bank excise tax was imposed by TCA 67-751, which provided in pertinent part:

> . . . each bank doing business in this state shall pay . . . an excise tax of three (3%) of the net earnings for the next preceding fiscal year. . .

The tax is reduced by certain ad valorum taxes, and the net earnings are to be calculated as are those for the corporate excise tax, that is, on federal taxable income. The immediately following section of the code 67-752 provided for a minimum amount of the tax as follows:

> In no event shall *the tax imposed under Sec. 67-751* upon any bank be less than an ad valorem tax calculated on the basis of sixty percent (60%) of the book value of the bank as of December 31, 1976. . . The book value of any bank shall be the sum of the paid in capital, surplus and individed profits. (Emphasis added.)

Defendants urge that the disputed bank excise taxes may be found valid under 67-752, because it bases the minimum tax on book value which would include both state and federal obligations, and is thus non-discriminatory within the meaning of Section 742. Alternatively, the de-

fense urges that the portion of book value attributable to federal securities may be excluded so as to eliminate any taxation of federal securities in the manner recently approved by the United States Supreme Court in *First National Bank of Atlanta* vs. *Bartow*, _____US _____, 84 LEd 535, 105 S. Ct. 1516 (1985). These proposed applications of 67-752 will not render the taxes valid. The bank excise tax is imposed by T.C.A. 67-751 as recognized by the above emphasized language in T.C.A. 67-752, so that 67-752 has only the effect of raising the total amount of the taxes calculated under 67-751 against federal taxable income in the event the 67-751 calculation is lower than the 67-752 calculation. Thus, the minimum is still calculated against federal taxable income, which includes federal security income and not state security income. This violates the non-discrimination provision of Section 742. The *Bartow* cases [sic] does not address this problem, because it does not involve discrimination between federal and state securities under the exception in Section 742, but rather the need to satisfy the general prohibition in Section 742: the total prohibition of taxation of federal securities.

The defense suggestions would require an application of the taxing statute contrary to its express provisions, in particular, contrary to the clearly expressed intent of 67-752 that the tax is imposed under 67-751. While Tennessee courts may determine the meaning of Tennessee law, a state statute which expressly violates Section 742 cannot be given a meaning contrary to its express language so that discriminatory taxation will appear not to occur. The taxation question involved is very complex. Even were the judiciary to take on the legislative task of responding to the effects of the *Garner* case, the result might not be in accord with the legislative intent at all. Here, for example, when the overall effect of the *Garner* ruling was considered and acted upon legislatively, the end result was to eliminate the bank excise tax altogether. When the Tennessee Supreme Court considered *Garner* (624 SW2d 551),

before its appeal to the United States Supreme Court, the necessary implication of its ruling at that time was that the Legislature intended to include federal obligations in the calculation of the bank excise tax. Thereafter, on remand in *Garner* the Tennessee Supreme Court interpreted that act in accord within the fair import of its language, and did not declare the entire act invalid or elide the portion of the act exempting Tennessee securities. Analogously, the act should not be read to exclude consideration of federal securities, where it expressly provides for the opposite.

The second major claim made by Plaintiff is that the assessment of the corporate excise taxes under TCA 67-2701 et seq. (now 67-4-801 et seq.) for the years 1982 and 1983 were invalid. For the same reasons the 1982 bank excise tax assessments were invalid, the 1982 corporate excise tax assessments are also invalid, and may be recovered. The corporate excise tax, based upon the bank's federal taxable income, which included income from federal but not state securities, impremissibly discriminates against federal securities in violation of Section 742. *Memphis Bank and Trust Co.* vs. *Garner,* supra.

The defense urges that the corporate taxes or a portion of them may be found validity [sic] imposed by excluding from consideration the net amount of income from federal securities. This may not be done because a substantial portion of federal security income would still be considered in the tax calculation (that portion not allocated to net income), while no Tennessee security income would be considered. A higher tax will thus result due to the consideration of income on federal securities to the extent it offsets expenses, while at the same time income from Tennessee securities not being considered does not offset expenses. The practical effect of this is to increase the tax by reason of the discriminatory consideration of federal obligations. It is observed that what the defense proposes is contrary to the express language of the taxing statue

as has been discussed with respect to the bank excise tax, and here too creates the same type of problems in determining legislative intent.

There remains the question of whether the 1983 corporate excise taxes were validly imposed. In 1983 the Legislature amended the corporate excise tax to include the consideration of Tennessee obligations. This eliminated the discrimination prohibited by Section 742. In the *Garner* case the United States Supreme Court noted that it did not reach the question of whether the Tennessee bank excise tax, which was essentially the same kind of tax as the corporate excise tax, was a franchise or other nonproperty tax within the meaning of Section 742 so as to permit nondiscriminatory taxation. *Memphis Bank and Trust Co.* vs. *Garner,* supra, at 567, FN 6. However, it was necessarily the ruling of the Tennessee Supreme Court prior to the appeal to the United States Supreme Court (624 SW2d 551) that the Tennessee bank excise tax was such a "franchise as other nonproperty tax." Were this not true, the exception for nondiscriminatory taxes in Section 742 could not have been applicable, and the question of nondiscriminatory taxes would not have had to have been considered. The ruling of the Tennessee Supreme Court in *Garner* that the basic tax was a franchise tax within the meaning of the Section 742 exception should and will be followed with respect to the corporate excise tax. Nothing in any of the United States Supreme Court decisions called to the attention of this court compels a different finding. Accordingly, it is concluded the 1983 corporate excise taxes at issue here were properly imposed.

Argument is made on behalf of Plaintiff that TCA 9-9-112, prohibiting taxation of state bonds, prohibits the inclusion of such Tennessee securities held by banks in the determination of the corporate excise tax. The corporate excise tax is on the privilege of doing business in corporate

form. Measuring that tax by income from Tennessee obligations does not constitute taxation of the bonds themselves, and is not inconsistent with imposition of the corporate tax. *Memphis Bank and Trust Co.* vs. *Garner* 624, SW2d 551 (Tenn 1981); *National Life and Accident Ins. Co.* vs. *Dempster,* 168 Tenn 446, 79 SW 2d 564 (1935).

Finally, the corporate excise tax as amended does not violate the constitutional prohibition against impairment of obligation of a contract. The tax is upon the exercise of corporate privilege, and this is true even though the privilege as exercised includes the acquisition and enjoyment of nontaxables. *Pacific Co.* vs. *Johnson,* 285 US 480, 76 LED 893, 52 S. Ct. 424 (1932); *Connecticut Bank and Trust Co.* vs. *Tax Comm.* 423 As 2d 883 (Conn. 1979); *Nat'l Bank of Alaska* vs. *State Dept. of Rev.* 642 P 2d 811 (Alas. 1982).

By way of summary Plaintiff may recover the 1982 bank and corporate excise taxes, but not the 1983 corporate excise taxes. The tax statutes in effect in 1982 discriminated on their face against federal securities, and the suggestions of the defense do not avoid that effect, while the 1983 amendment to the corporate excise tax does. A judgment in accord herewith, and incorporating this opinion by reference may be entered. Costs are taxed against Defendants.

Enter this the 28th day of January, 1986.

/s/Frederick McDonald
CHANCELLOR

cc:

Dale Workman
John Batson
Joe Peel
Mike Swiney
James Gooch
Steven Rush

IN THE CHANCERY COURT
FOR KNOX COUNTY TENNESSEE PART I

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE (PARK NATIONAL BANK)

VS. No. 78471

MARTHA B. OLSEN, Commissioner
of Revenue for the State of
Tennessee, et al

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE (FIRST AMERICAN BANK
OF KNOX COUNTY)

VS. No: 79581

ROBERT BROOME, Knox County
Trustee, et al

MEMORANDUM OPINION

Plaintiff First American National Bank of Knoxville has moved for prejudgment interest. Under T.C.A. 67-1-904 interest as the court may determine to be proper, not exceeding the legal note, may be allowed. Plaintiff paid the disputed taxes under protest in February 1983, after *Memphis Bank and Trust Co.* vs. *Garner,* 459 US 392 (1983), which raised a serious question as to the validity of the taxes, had been decided. Plaintiff has been denied the use of the funds ever since. It would not be equitable that the taxing authorities have the use of the funds for so long without some charge. It is concluded that Plaintiff shall be allowed 7% interest on the involved funds.

Various questions are raised by the taxing authorities, which upon careful review, are found to be without merit. Revival of the predecessor taxing statutes is requested. This is not proper, because (1) the involved statute was

not held unconstitutional, only its application was, and (2) consistent with this conclusion (if not controlling authority) is the ruling of the Tennessee Supreme Court in *Memphis Bank and Trust Co.* case. This case is not deemed to be an appropriate situation to deny what Defendant's call a retroactive application, because the federal law at all times prohibited the attempted taxation, and in any event, the attempted collection of the tax occurred after the decision in *Memphis Bank and Trust Co.*, supra, so no retroactivity is involved here.

The Defendants reargue the effect of the *First National Bank of Atlanta,* v. *Bartow,* _____US _____84 LEd 535, 105 S. Ct. 1516 (1985). *Bartow* (a bank stock tax case) approved a consideration of the value of federal securities in calculating a state tax on net worth (value), because the value of state securities was also included in determining net worth, and this resulted in no discrimination between federal and state securities. In the instant case the minimum tax by the terms of the statute (T.C.A. 67-751 and 67-752) cannot be determined without consideration of federal security income while at the same time excluding consideration of state security income. This occurs, because a calculation under both section 67-751 and section 67-752 must be made to determine which section results in the higher tax, with the higher tax then being imposed. This puts federal securities at a significant disadvantage to state securities, resulting in prohibited discrimination under 31 USC, Section 742. The discriminatory disadvantage to federal securities occurs, because as a bank's income from federal securities increases so as to push the bank's income toward or above the level of the minimum tax (above which a higher tax under 67-751 results), the purchase of state securities, whose income will not increase the bank's income so as to move it toward or above the minimum tax level, will be more attractive than the purchase of federal securities. Put another way, the purchase of state securities, which do not go to cause

any higher tax than the minimum tax provided for in 67-752, is a better buy for a bank than federal securities, whose income does go to trigger a tax higher than the minimum tax. The advantage in buying state securities increases more and more as the bank's income approaches and goes higher than the minimum tax level. It should be observed that a purchase of state securities will generally not raise the minimum tax level, because that tax is based on asset value, and the purchase of state securities for purposes of the tax would merely be an exchange of one asset (cash) for another asset (state securities), and this would not affect the total of the bank's assets, including its net worth upon which the minimum tax is based.

It is urged by the taxing authorities that Plaintiff Bank does not have standing to maintain this action, and that Plaintiff is not adversely affected by the tax. A state may not deny an individual the right to assert its rights under federal law on the theory of lack of standing to do so, and should Plaintiff not be allowed to assert its rights here, the intended effect of 31 USC 742 would be greatly thwarted. Finally, to urge that Plaintiff Bank is not adversely affected in the face of the attempted imposition of the disputed taxes is not supported by the facts, since if Plaintiff is denied recovery, it will pay a very significant amount of taxes that it would not otherwise have to.

An order in accord with this opinion, and incorporating it by reference may be entered.

Enter this the 8th day of May, 1986.

/s/Frederick McDonald
CHANCELLOR

cc:

Dale Workman
Michael Swiney
Steve Rush

John Batson
Joe Peel
Robert Akard

IN THE CHANCERY COURT
FOR KNOX COUNTY, TENNESSEE

FIRST AMERICAN NATIONAL OF KNOXVILLE (PARK NATIONAL BANK), -

Plaintiff

v. No. 78471

MARTHA B. OLSEN, Commissioner of Revenue for the State of Tennessee, et al,

Defendants

FIRST AMERICAN NATIONAL BANK OF KNOXVILLE (FIRST AMERICAN BANK OF KNOX COUNTY),

Plaintiff

v. No. 79581

ROBERT BROOME, Knox County Trustee, et al,

Defendants

JUDGMENT

These two consolidated cases were heard before the Honorable Frederick D. McDonald, Chancellor for the Knox County Chancery Court, Part I, on September 30, 1985 and October 1, 1985. The Court filed its Memorandum Opinion on January 28, 1986 on the trial of this matter. After the filing of the Court's Memorandum Opinion, the following motions were filed:

1. Plaintiffs' Motion For Additional Findings Of Fact And Conclusions Of Law;

2. Defendant Broom's and Palmer's Motion For Further Findings; and

3. Defendant Olsen's Motion To Reconsider And To Make Additional Findings Of Fact And Conclusions Of Law.

The Memorandum Opinion of this Court on these various motions was filed on May 8, 1986, granting the plaintiffs' motion in part, and denying the defendants' motions.

On the pleadings heretofore filed by the parties and after hearing the testimony of witnesses in open Court, the argument of counsel, and reviewing the exhibits of the parties, it appears to the Court that the suits against the City of Knoxville and Knox County are well taken and that the suit against the defendant Martha B. Olsen is well taken in part. The Memorandum Opinion of the Court filed January 28, 1986 with corrected pages 4 and 5 and the Memorandum Opinion of this Court dated May 8, 1986 are incorporated by reference into this judgment as fully as if they were set forth in their entirety.

It is therefore ORDERED, ADJUDGED and DECREED that the plaintiffs are granted a judgment against the defendants as follows:

1. In Docket No. 79581, plaintiff is granted judgment against (a) Robert Broome, Knox County Trustee, in the amount of $8,878.81 plus prejudgment interest computed at the rate of seven percent for a total judgment against this defendant of $10,898.32, and (b) Carol Palmer, Treasurer of the Finance Department of the City of Knoxville, in the amount of $10,725.56 plus prejudgment interest computed at the rate of seven percent for a total judgment against this defendant of $13,165.11.

2. In Docket No. 78471, the plaintiff is granted judgment against (a) Robert Broome, Knox County Trustee, in the amount of $44,224.01 plus prejudgment interest computed at the rate of seven percent for a total judgment against this defendant of $54,282.85, (b) Carol Palmer, Treasurer of the Finance Department of the City of Knoxville, in the amount of $59,023.73 plus prejudgment interest computed at the rate of seven percent for a total judgment against this defendant of $72,448.79, and (c) Martha B. Olsen, Commissioner of Revenue of the State

of Tennessee, in the amount of $160,456.00 plus prejudgment interest computed at the rate of seven percent for a total judgment against this defendant of $199,293.12. All costs attributable to this cause are taxed against the defendants.

Enter this the 29th day of May, 1986.

/S/FREDERICK D. MCDONALD
FREDERICK D. MCDONALD
CHANCELLOR

APPROVED FOR ENTRY:

/s/D. MICHAEL SWINEY
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Nashville, TN 37219

SUPREME COURT OF TENNESSEE, AT KNOXVILLE
SEPTEMBER TERM 1987

Filed November 23, 1987
Robert W. Summar, Clerk

DECREE

FIRST AMERICAN NATIONAL BANK OF KNOXVILLE (PARK NATIONAL BANK. Plaintiff-Appellant	Knox Equity
VS.	(No. 78471)
MARTHA B. OLSEN, COMMISSIONER OF REVENUE FOR THE STATE OF TENNESSEE. Defendant-Appellee	Affirmed And Remanded

This cause coming on to be heard upon a transcript of the record from the Chancery Court of Knox County, briefs of the parties, and oral argument of counsel, upon consideration whereof the Court is of the opinion that in the decree of the Chancellor there is no error.

It is therefore ordered and decreed by the Court that the judgment of the trial court is affirmed and this cause is remanded to the Chancery Court of Knox County for such further proceedings as may be necessary consistent with the Opinion of this Court, a copy of which shall accompany the mandate on the remand to the trial court.

Costs are adjudged against the Plaintiff, First American National Bank of Knoxville (Park National Bank), and execution may issue from this Court for the costs incident to the appeal. This cause is remanded to the trial court aforesaid for collection of the costs adjudged therein.

Frank F. Drowota, III., J.
William J. Harbison, C.J.
Robert E. Cooper, J.
Charles H. O'Brien, J.
Ben H. Cantrell, Sp. J.

IN THE SUPREME COURT OF TENNESSEE
AT KNOXVILLE

FIRST AMERICAN NATIONAL BANK
OF KNOXVILLE (PARK NATIONAL
BANK),

Plaintiff-Appellant,

v. No. 270

MARTHA B. OLSEN,
Commissioner of Revenue for
the State of Tennessee,

Defendant-Appellee.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

(Date Filed: January 15, 1988)

Notice is hereby given that First American National Bank of Knoxville (Park National Bank), the appellant above-named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of Tennessee, affirming the decision of the Chancery Court of Knox County upholding the validity of the Tennessee Excise Tax, Tenn. Code Ann., sections 67-4-801 to 67-4-820, entered into this action on November 23, 1987.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

PAINE, SWINEY, AND TARWATER
By /s/D. MICHAEL SWINEY
Donald F. Paine
D. Michael Swiney
T. Harold Pinkley
Counsel for Appellant
700 Burwell Building
602 S. Gay Street
Post Office Box 198
Knoxville, TN 37901
(615) 525-0880

CERTIFICATE OF SERVICE

I, D. Michael Swiney, a member of the Bar of the Tennessee Supreme Court and of the Bar of the United States Supreme Court, hereby certify on the 13th day of January, 1988, a copy of the foregoing Notice of Appeal to the Supreme Court of the United States was mailed, first class postage prepaid, to:

Joe C. Peel, Esq.
Office of the Attorney General
450 James Robertson Parkway
Nashville, Tennessee 37219

Attorney for Appellee,
W. J. Michael Cody
Attorney General for the
State of Tennessee.

I further certify that all parties required to be served have been served.

PAINE, SWINEY, AND TARWATER

By: D. MICHAEL SWINEY
D. Michael Swiney
700 Burwell Building
602 S. Gay Street
Post Office Box 198
Knoxville, TN 37901
(615) 525-0880

Counsel for Appellant

TITLE 67, TENNESSEE CODE ANNOTATED

(Corporate Franchise Tax)

67-4-903. Corporations subject to tax.—(a) All corporations, cooperatives, joint-stock associations, and business trusts, including regulated investment companies and real estate investment trusts, organized for profit under the laws of this state or any other state or country and doing business in Tennessee, including state chartered banks and national banks doing business in Tennessee shall, without exception other than as provided herein, pay to the commissioner of revenue, annually a privilege tax in addition to all other taxes, the rate and measure of which are hereinafter set forth. The tax shall be paid for the privilege of engaging in business in corporate form in this state and shall be in addition to all other taxes levied by any other statute.

(b) Every such taxable entity organized and existing under and by virtue of the laws of this or any other state, territory or country, or organized and existing without any specific statutory authority, now or hereafter doing business within this state, without domesticating or qualifying to do business in this state, or while its charter is forfeited, revoked or suspended, shall as a recompense for the protection of its local activities and as compensation for the benefits it receives from doing business in Tennessee, pay the tax imposed by this part.

(c) The tax imposed by this part shall apply to corporations whose business is being conducted by a receivership or trusteeship appointed by any court of competent jurisdiction and shall continue to accrue until such time as the corporation has been actually and legally dissolved or withdrawn from this state.

(d) There shall be exempt from the payment of the tax levied under this part any corporation organized under the laws of the state of Tennessee whose sole expressed cor-

porate purpose is for the furthering of industrial development in communities throughout the state, and doing related matters thereto, and whose stockholders receive no income other than interest or dividends on money invested in said corporation for constructing industrial buildings and whose officers receive no compensation.

67-4-904. Rate of tax.—(a) The privilege tax hereby imposed shall be a tax of twenty-five cents (25¢) on the one hundred dollars ($100), or major fraction thereof, of the issued and outstanding stock, surplus and undivided profits of each such corporation as shown by the books and records of such corporation at the close of its last fiscal year preceding the making of the sworn report hereinafter required.

(b) For purposes of this section "issued and outstanding" stock shall not include treasury stock.